

II. EXECUTIVE SUMMARY

A. Principles

21. Section 254(b) sets forth the principles that are to guide the Commission in establishing policies for the preservation of universal service. These principles include:

- (1) quality services should be available at just, reasonable, and affordable rates;²⁴
- (2) access to advanced telecommunications and information services should be provided in all regions of the Nation;²⁵
- (3) consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas;²⁶
- (4) all providers of telecommunications services should make an equitable and non-discriminatory contribution to the preservation and advancement of universal service;²⁷
- (5) there should be specific, predictable and sufficient [f]ederal and [s]tate mechanisms to preserve and advance universal service;²⁸ and
- (6) elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services.²⁹

In addition, the Commission may consider such "additional principles" as the Commission and the Joint Board determine are necessary and appropriate for the protection of the public interest,

²⁴ 47 U.S.C. § 254(b)(1).

²⁵ 47 U.S.C. § 254(b)(2).

²⁶ 47 U.S.C. § 254(b)(3).

²⁷ 47 U.S.C. § 254(b)(4).

²⁸ 47 U.S.C. § 254(b)(5).

²⁹ 47 U.S.C. § 254(b)(6).

convenience and necessity and are consistent with the Act.³⁰ In addition to the principles specified in section 254(b), we agree with the Joint Board and adopt its recommendation that "competitive neutrality" should be among the principles that guide the universal service support mechanisms and rules. We adopt this principle and the principles enumerated by Congress in section 254(b) to preserve and advance universal service while promoting the pro-competitive goals of the 1996 Act.

B. Definition of Universal Service

22. Section 254(c)(1) requires the Commission to establish a definition of telecommunications services that will be supported by universal service support mechanisms. Based on the principles embodied in section 254, and guided by the recommendation of the Joint Board, we find that the definition of supportable services includes: voice grade access to the public switched network, with the ability to place and receive calls; Dual Tone Multifrequency (DTMF) signaling or its functional equivalent; single-party service; access to emergency services, including in some instances, access to 911 and enhanced 911 (E911) services; access to operator services; access to interexchange services; access to directory assistance; and toll limitation services for qualifying low-income consumers. As recommended by the Joint Board, eligible carriers must offer each of the designated services in order to receive universal service support. We find that, consistent with the Joint Board's recommendation, a carrier that currently is unable to provide single-party service may petition its state commission to receive universal service support for a designated period of time while the carrier completes the network upgrades needed to offer single-party service. Further, based on the Joint Board's recognition that some carriers currently may be unable to provide access to E911 service and toll limitation services, carriers may receive, for a specified period of time, universal service support while completing network upgrades required for them to offer these services. In addition, all business and residential connections that are currently supported will continue to be supported until the forward-looking methodology for high cost companies is operational. Finally, as recommended by the Joint Board, we will convene a Federal-State Joint Board to review the definition of universal service on or before January 1, 2001.

C. Affordability

23. Based on the Joint Board's recommendation, we conclude that states should monitor rates and non-rate factors, such as subscribership levels, to ensure affordability. We agree with the Joint Board that there is a correlation between subscribership and affordability and we further agree that joint examination by the Commission and the states of the factors that may contribute to low penetration is warranted in areas, such as insular areas, where subscribership levels are particularly low.

³⁰ 47 U.S.C. § 254(b)(7).

D. Carriers Eligible for Universal Service Support

24. We conclude that the plain language of section 214(e)(1) does not permit the Commission or the states to adopt additional criteria as prerequisites for designating carriers eligible telecommunications carriers. Therefore, consistent with the Joint Board's recommendation, we adopt the statutory criteria contained in section 214(e)(1) as the rules for determining whether a telecommunications carrier is eligible to receive universal service support. Pursuant to section 214(e), eligible carriers must offer and advertise all the services supported by federal universal service support mechanisms throughout their service areas using their own facilities or a combination of their own facilities and resale of another carrier's services. We interpret the term "facilities" in section 214(e)(1) to mean any physical components of the telecommunications network that are used in the transmission or routing of the services designated for support under section 254(c)(1). We conclude that our adoption of this interpretation strikes a reasonable balance between adopting a more expansive definition of "facilities," which would undermine the Joint Board's recommendation to exclude from eligibility a carrier offering universal service exclusively through resold services, and adopting a more restrictive definition of "facilities," which we fear would thwart competitive entry into high cost areas. In order to interpret the section 214(e) facilities requirement in a competitively neutral manner, we conclude that a carrier that offers the federally supported services through the use of unbundled network elements, in whole or in part, satisfies the facilities requirement of section 214(e). We adopt the Joint Board's recommendation that eligible carriers not be required to offer the supported services wholly over their own facilities because the statute allows an eligible carrier to offer those services through a combination of its own facilities and resale. We also find, as did the Joint Board, that section 214(e) precludes an eligible carrier from offering the supported services solely through resale in light of the statutory requirement that a carrier provide universal service, at least in part, over its own facilities. Furthermore, consistent with the Joint Board's recommendation, we find that no additional measures are necessary to implement the provisions of section 254(e), which limit the purposes for which universal service funds may be used.

25. We agree with the Joint Board that the statute affords state commissions the primary responsibility for designating service areas served by non-rural carriers. We also concur in the Joint Board's finding, however, that states should exercise this authority in a manner that promotes the pro-competitive goals of the 1996 Act as well as the universal service principles of section 254. We therefore agree with the Joint Board that states should not designate service areas that are unreasonably large because unreasonably large service areas will discourage competitive entry by increasing the expenses associated with such entry. For similar reasons, and to promote competitive neutrality, we also recommend that state commissions not designate service areas that are based on ILECs' study areas. The Act treats service areas served by rural telephone companies differently from non-rural service areas. Section 214(e)(5) requires a service area served by a rural telephone company to be that company's existing study area, unless the states and the Commission, after taking into account the findings of the Joint Board,

establish a different definition. To minimize potential procedural delays associated with the federal-state cooperation that is required to alter the definition of a service area served by a rural carrier, we establish expedited procedures by which the definition of such an area may be changed in accordance with section 214(e)(5). We agree with the Joint Board that retaining the study areas of rural telephone companies as rural service areas is generally consistent with section 214(e)(5), the policy objectives underlying section 254, and with our decision to use a rural ILEC's embedded costs to calculate that company's support under the modified existing high cost mechanisms. We nevertheless encourage states to consider disaggregating a non-contiguous service area of a rural telephone company into service areas composed of the contiguous portions of that area because some wireless carriers may be unable to provide service in non-contiguous service areas. We conclude that the Joint Board correctly recommended that no additional regulations are necessary, at this time, to designate carriers to serve unserved areas. To assist us in monitoring the status of unserved areas, we encourage state commissions to submit to the Commission reports detailing the status of unserved areas in their states.

E. High Cost Support

26. Consistent with the Joint Board's recommendation, we find that a cost methodology based on forward-looking economic cost should be used to calculate the cost of providing universal service for high cost areas because it best reflects the cost of providing service in a competitive market for local exchange telephone service. We believe that a cost methodology can be designed based upon such consistent assumptions as economic depreciation, forward-looking cost of capital, and forward-looking outside plant cost, including reasonable profits. We agree with the Joint Board that the cost methodologies presented to us thus far are not sufficiently reliable to be used to determine universal service support at this time. Because input values that would significantly impact the model outputs, such as the cost of electronic switches and digital loop carrier devices, have never been provided to the Commission, we cannot accept the models before us. In addition, both models lack a compelling design for distributing customers in a particular geographic area, and thus, we cannot develop a reliable model based on the synthesis of the models before us. Consequently, we will issue a Further Notice of Proposed Rule Making (FNPRM) to establish a forward-looking universal service support mechanism based on forward-looking economic cost for non-rural carriers. We anticipate that we will adopt a forward-looking mechanism for non-rural carriers by August 1998, and that it will take effect on January 1, 1999. That mechanism will allow a state either to use the Commission's cost methodology or develop its own cost study, within the guidelines that we will establish, to determine the level of universal service support for carriers in that state. Until the forward-looking mechanism takes effect on January 1, 1999, non-rural carriers will continue to receive high cost loop support and LTS based on the existing universal service mechanisms. As recommended by the state members of the Joint Board, rural carriers will continue to receive support based on their embedded cost using the current mechanisms with some modifications. We will continue to work with the Joint Board regarding the development of appropriate forward-looking economic cost mechanisms for rural carriers. As recommended

by the Joint Board, we will also continue to explore the use of competitive bidding as a mechanism to provide universal service.

F. Support for Low-Income Consumers

27. We adopt the Joint Board's recommendations to make three broad categories of changes to the Lifeline and Link Up programs so that they better comport with our universal service principles and the 1996 Act's renewed concern for low-income consumers. First, we agree with the Joint Board's recommendation to expand Lifeline to make it available in all states, territories, and commonwealths of the United States, modify the state matching requirement, and increase the federal Lifeline support amount. We find that these modifications comply with the principles in sections 254(b)(1) and (3), respectively, that rates should be "affordable" and access should be provided to "low-income consumers" in all regions of the nation. Second, we adopt the Joint Board's recommendation to make the contribution and distribution of low-income support competitively and technologically neutral by requiring equitable and nondiscriminatory contributions from all providers of interstate telecommunications services, consistent with sections 254(d) and (e), and allowing all eligible telecommunications carriers to receive support for offering Lifeline and Link Up service. Third, we adopt the Joint Board's recommendation to provide low-income consumers with access to certain services and policies.

28. Specifically, we agree with the Joint Board that Lifeline consumers should have access to the same services as those supported in rural, insular, and high cost areas: voice grade access to the public switched network, with the ability to place and receive calls; DTMF signaling or its functional equivalent; single-party service; access to emergency services, including in some circumstances, access to 911 and E911; access to operator services; access to interexchange services; and access to directory assistance. In determining the specific services to be provided to low-income consumers, we adopt the Joint Board's reasoning that section 254(b)(3) calls for access to services for low-income consumers in all regions of the nation, and that universal service principles may not be realized if low-income support is provided for service inferior to that supported for other subscribers. In addition, we agree with the Joint Board that Lifeline service should include toll-limitation services, at the customer's request, to the extent that carriers are capable of providing them. We agree with the Joint Board that toll-limitation services will help low-income consumers control their toll bills and consequently be better able to maintain access to telecommunications services, as section 254(b)(3) envisions. We concur with the Joint Board's recommendation to prohibit the disconnection of local service for non-payment of charges incurred for toll calls. We are persuaded by the Joint Board's reasoning that such a rule will help improve subscribership among low-income consumers, based on studies indicating that disconnection for non-payment of toll charges is a significant cause of low subscribership among low-income consumers. We therefore believe that this rule advances the principles of section 254(b) that rates should be "affordable" and access to telecommunication services should be provided to "low-income consumers." We further find, as did the Joint Board, that local and toll services are distinct services, and therefore carriers

providing toll service should take action against consumers who do not pay their toll bills. We also adopt the Joint Board's recommendation to prohibit carriers from requiring service deposits from Lifeline customers who elect toll blocking. Service deposits, which primarily serve to guard against uncollectible toll charges, deter subscribership among low-income consumers and thus run counter to the principle in section 254(b)(3) that low-income consumers should have access to telecommunications services. We therefore find, as did the Joint Board, that consumers who receive toll blocking, which bars the placement of toll calls, should be able to benefit from a rule prohibiting service deposits.

G. Support for Schools and Libraries

29. We concur with the Joint Board's recommendation to provide schools and libraries with discounts on all commercially available telecommunications services, Internet access, and internal connections. This program provides schools and libraries with the maximum flexibility to purchase the package of services they believe will meet their communications needs most effectively. We conclude that sections 254(c)(3) and 254(h)(1)(B) authorize us to permit eligible schools and libraries to receive telecommunications services, Internet access, and internal connections at discounted rates from telecommunications carriers. Because we share the Joint Board's preference that we foster competition from non-telecommunications carriers, we encourage those non-carrier providers to enter into partnerships or joint ventures with telecommunications carriers in order to provide services to schools and libraries. In addition, we adopt the Joint Board's recommendation to provide discounts for Internet access and internal connections provided by non-telecommunications carriers. We adopt this recommendation under the authority of sections 254(h)(2)(A) and 4(i).

30. We agree with the Joint Board's finding that fiscal responsibility compels us to require schools and libraries to seek competitive bids for all services eligible for section 254(h) discounts. Competitive bidding is the most efficient means for ensuring that schools and libraries are informed about all of the choices available to them. In addition, we agree with the Joint Board that the lowest corresponding price, defined for each telecommunications carrier bidding to serve a school or library as the lowest price that carrier charges to similarly situated non-residential customers in its geographic service area for similar services, shall constitute the ceiling for that carrier's competitively bid pre-discount price for interstate rates. We would expect state commissions to require the same for intrastate rates. In areas in which there is only one bidder, that bidder's lowest corresponding price would constitute the pre-discount price.

31. We concur with the Joint Board's recommendation that we adopt discounts from 20 percent to 90 percent for all telecommunications services, Internet access, and internal connections, with the level of discounts correlated to indicators of poverty and high cost for schools and libraries. This approach satisfies section 254(h)(1)(B)'s directive that the discount be an amount that is "appropriate and necessary to ensure affordable access to and use of" the services eligible for the discount, and fulfills our statutory obligation to create specific,

predictable, and sufficient universal service support mechanisms. We also adopt the Joint Board's recommendation to establish an annual cap of \$2.25 billion on the amount of funds available to schools and libraries.

32. We agree with the Joint Board that all schools falling within the definition contained in the Elementary and Secondary Education Act of 1965 and meeting the criteria of section 254(h), whether public or private, shall be eligible for universal service support. In light of an amendment to section 254(h)(4), enacted in late 1996, we found it necessary to look anew at the definition of library and adopt a definition that is consistent with the directives of section 254(h). We, therefore, adopt the definition of library contained in the Library Services and Technology Act for purposes of section 254(h), but we also conclude that a library's eligibility for universal service funding will depend on its funding as an independent entity. This independence requirement is consistent with both congressional intent and the expectation of the Joint Board that universal service support would flow to an institution of learning only if it is either an elementary or secondary school.

33. We agree with the Joint Board that schools and libraries should be permitted to participate in consortia for purposes of aggregating their demand with others. Because of concerns raised in comments received after adoption of the Recommended Decision that permitting large private sector firms to join with eligible schools and libraries to seek prices below tariffed rates could compromise both federal and state policies of non-discriminatory pricing, we adopt a slightly modified version of the Joint Board recommendation on consortia. We conclude, therefore, that eligible schools and libraries participating in consortia may receive universal service support only if such consortia are composed of other eligible schools and libraries, eligible health care providers, and ineligible public sector (governmental) members. Eligible schools and libraries participating in consortia that include ineligible private sector members will not be eligible to receive universal service discounts unless the pre-discount prices of any interstate services that such consortia receive from ILECs are generally tariffed rates. We conclude that this approach satisfies both the purpose and the intent of the Joint Board's recommendation because it should allow the consortia containing eligible schools and libraries to aggregate sufficient demand to influence existing carriers to lower their prices and should promote efficient use of shared facilities. We also agree with the Joint Board's recommendation that we interpret section 254(h)(3) to restrict any resale whatsoever of services purchased pursuant to a section 254(h) discount.

34. We concur with the Joint Board's finding that Congress intended to require accountability on the part of schools and libraries. We agree, therefore, with the Joint Board's recommendation that eligible schools and libraries be required to: (1) conduct internal assessments of the components necessary to use effectively the discounted services they order; (2) submit a complete description of services they seek so that it may be posted for competing providers to evaluate; and (3) certify to certain criteria under penalty of perjury.

H. Support for Health Care Providers

35. Sections 254(c) and 254(h) add health care providers to the list of entities that may benefit from universal service support. Recognizing that section 254 requires that universal service support mechanisms be specific, predictable, and sufficient, we establish support for health care providers subject to a \$400 million annual cap. Section 254(h)(1)(A) provides that a health care provider that serves persons who reside in rural areas shall receive telecommunications services necessary for the provision of health care services in a state at rates that are reasonably comparable to those charged for similar services in urban areas in that state. Because section 254(h)(1)(A) specifies that the calculation of the credit for carriers providing the service is to be based on the difference between rates in "comparable rural areas," and the rates charged to the health care provider, we, consistent with the Joint Board recommendation, provide support under this section for telecommunications services for all public and not-for-profit health care providers located in rural areas. Any telecommunications service of a bandwidth capacity up to and including 1.544 Megabits per second (Mbps) that is necessary for the provision of health care services is eligible for support, but there are limits on the services that each rural health care provider may obtain. Telecommunications carriers must charge eligible rural health care providers a rate for each supported service that is no higher than the highest tariffed or publicly available commercial rate for a similar service in the closest city in the state with a population of 50,000 or more people, taking distance charges into account.

36. Section 254(h)(2)(A) directs the Commission to establish "competitively neutral rules to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and nonprofit health care providers." To meet the goals of this section, and, based on our review of comments filed in response to the Recommended Decision, we adopt mechanisms to provide support for limited toll-free access to an Internet service provider. Each health care provider that lacks toll-free access to an Internet service provider may receive the lesser of the toll charges incurred for 30 hours of access to an Internet service provider or \$180 per month in toll charge credits for toll charges imposed for connecting to the Internet.

37. Carriers providing supported telecommunications services to health care providers will be entitled to treat the amount eligible for support as an offset against their annual universal service obligation and receive a reimbursement for any amount by which the support due the carrier exceeds the obligation in any one year. Non-telecommunications providers providing supported services to health care providers will receive direct reimbursement for the eligible amount.

I. Interstate Subscriber Line Charge/Carrier Common Line Charges

38. We adopt the Joint Board's conclusion that LTS must be removed from carrier common line (CCL) charges. This change will be effectuated in the access charge reform

proceeding. Consistent with the Joint Board's recommendation, we provide for payments similar to LTS out of the new universal service support mechanisms to rural telephone companies that currently receive LTS or competitors that win subscribers from such carriers. Consistent with the Joint Board's recommendation, we maintain the current \$3.50 cap on the SLC for primary residential and single-line business lines.

J. Administration of Support

39. Section 254(d) states that all carriers that provide interstate telecommunications services must contribute to universal service support mechanisms in an equitable and nondiscriminatory manner. To ensure that all providers of similar services make the same contributions to universal service, we adopt the Joint Board's recommendation that all telecommunications carriers that provide interstate telecommunications services must contribute to the support mechanisms and we issue a list of examples of interstate telecommunications services. In addition, we find that the public interest requires providers of interstate telecommunications on a non-common carrier basis and payphone aggregators to contribute to the support mechanisms pursuant to the Commission's permissive authority over "other providers of interstate telecommunications." We adopt the Joint Board's recommendation that contributors whose contribution would be less than the administrator's administrative cost of collecting the contribution will be exempt from contribution and reporting requirements under the *de minimis* exemption contained in section 254(d).

40. Consistent with the Joint Board, we adopt a contribution assessment methodology that is competitively neutral and easy to administer. Contributions will be assessed against end-user telecommunications revenues, revenues derived from end users for telecommunications and telecommunications services, including SLCs. We adopt the Joint Board's recommendation that support for the programs for schools, libraries, and rural health care providers be assessed based on interstate and intrastate telecommunications revenues. Because the Joint Board did not issue a recommendation regarding the revenue base for the balance of the support mechanisms, we will maintain historic jurisdictional lines and will assess contributions for support for the high cost and low-income programs on interstate telecommunications revenues.

41. Because the Joint Board did not address how contributors would recover their universal service contributions, we maintain historic jurisdictional lines and permit recovery of universal service contributions through the contributing carrier's interstate rates. For ILECs subject to price caps, we will permit universal service contributions to be added to the carrier's common line basket, and recovered in the same manner as common line charges.

42. Finally, we adopt the Joint Board's recommendation to appoint the National Exchange Carrier Association (NECA) the temporary administrator of the support mechanisms, subject to changes in NECA's governance that render it more representative of non-ILEC interests. Consistent with the Joint Board, we shall also create a Federal Advisory Committee to

recommend a neutral, third-party permanent administrator of the support mechanisms. We require the administrators to administer the support mechanisms in a neutral and equitable manner, and to keep all support monies separate from all other funds under the control of the administrator or temporary administrator.